TENNESSEE DEPARTMENT OF REVENUE
REVENUE RULING 07-13

WARNING

Revenue rulings are not binding on the Department. This presentation of the ruling in a redacted form is information only. Rulings are made in response to particular facts presented and are not intended necessarily as statements of Departmental policy.

SUBJECT

Obligation of an out-of-state Taxpayer to collect use tax from a Tennessee customer.

SCOPE

Revenue Rulings are statements regarding the substantive application of law and statements of procedure that affect the rights and duties of taxpayers and other members of the public. Revenue rulings are advisory in nature and are not binding on the Department.

FACTS

The Retailer (hereinafter the "Taxpayer"), a C Corporation, is organized and located outside the State of Tennessee. The Taxpayer's business activity within the state of Tennessee consists of solicitation of sales of printed clinical research materials to for-profit and not-for-profit pharmaceutical entities (end users) to be utilized in drug studies, clinical trials and other informational uses. The clinical research materials can be delivered in the form of loose-leaf pages, folders, or threefold pamphlets. The Taxpayer's customers provide text information and a description of the required layout or format for the clinical research materials to be printed. The Taxpayer subsequently provides the composition, printing service including supplies, binding if necessary, and any required packaging.

Customer orders are in almost all instances printed in one lot instead of on an "as needed" basis. Upon completing the order, the customer is billed for the entire contract price regardless of whether the product is immediately shipped or subsequently stored in the Taxpayer's warehouse. Due to the nature of clinical research and drug studies, the customer is not able to immediately determine when or where the product stored in the Taxpayer's warehouse may be required to be shipped.

Any customer order shipped in one lot (no storage) will be shipped Free On Board (F.O.B.) the Taxpayer's loading dock. Any order where the product is not immediately shipped will be stored in the Taxpayer's climate controlled warehouse outside of

Tennessee at no additional charge. During the period of storage, the Taxpayer will insure the product against damage or loss. Legal title, however, passes to the customer once the order has been completed and the customer has been billed. Since legal title has passed to the customer, any product stored by the Taxpayer is not inventory on the books of the Taxpayer. The period of storage may range from several days to several years with subsequent shipments occurring at the direction of the customer. The Taxpayer's distribution policy for stored products requires a formal written release from the customer with the handling fees and the shipping charges separately itemized and billed for any product shipped. The customer will only be charged for shipping and/or handling on shipments of the product subsequent to the initial shipment. Shipments are via common carrier as arranged by the Taxpayer. Any products in the warehouse, without activity for an extended period of time, may be destroyed upon confirmation from the customer.

ISSUES

1. Is the Taxpayer required to collect and remit Tennessee sales or use tax on the initial shipment of product sold to the Tennessee end user?

2. Is the Taxpayer required to collect and remit sales or use tax on the subsequent shipments of research materials, as it is not known at the initial time of sale when, where, or to whom the research materials will be delivered?

3. Is the Taxpayer required to collect and remit Tennessee sales tax on the shipping and handling charges for either the initial shipment or subsequent shipments which may occur up to several years after the initial sales transaction?

RULINGS

1. The Taxpayer is required to collect and remit use tax on any shipments sent to a customer in Tennessee.[1] However, any sales tax legally paid to the Taxpayer's home state will be credited against any Tennessee tax liability.

2. The Taxpayer is required to collect and remit use tax on any subsequent shipments of research materials to customers in Tennessee. The tax for each set of materials delivered to Tennessee should be collected and remitted at the time when the customer requests shipment to Tennessee and when the Taxpayer charges the customer for shipping and handling for the shipment to Tennessee.

3. The Taxpayer is not required to collect and remit Tennessee sales tax on the shipping charges for any of the shipments as long as the shipping charges are stated separately from any handling fees. The Taxpayer is required to collect and remit Tennessee sales tax on any handling fees.

[1] Sales to certain not-for-profit entities are exempt if all requirements of Tenn. Code Ann. § 67-6-322 are met.

ANALYSIS

1. The Taxpayer is required to collect and remit use tax on any shipments sent to a customer in Tennessee. However, any sales tax legally paid to the Taxpayer's home state will be credited against any Tennessee tax liability.

The Retailers' Sales Tax Act imposes tax on the privilege of selling goods at retail in Tennessee or purchasing goods out of state for use in Tennessee. Tenn. Code Ann. § 67-6-201. If goods are brought within the State of Tennessee for sale at retail, use, consumption, distribution or storage for subsequent use, they are subject to the taxing power of the State. *Texas Gas Transmission Corp. v. Benson*, 444 S.W.2d 137, 139 (Tenn. 1969).

In order for the Taxpayer, an out-of-state seller, to be required to collect and remit a use tax as a dealer, there must be a sufficient nexus between the Taxpayer and the State of Tennessee. *Pearle Health Services v. Taylor*, 799 S.W.2d 655 (Tenn. 1990). The Taxpayer has represented that it solicits sales in Tennessee. More details are needed to determine if the solicitation of sales is such as to give the Taxpayer nexus with Tennessee. For example, the Taxpayer will have nexus with Tennessee if it sends sales people, either employees or independent contractors, to Tennessee for the purpose of attracting, soliciting and obtaining Tennessee customers. *See Scripto, Inc. v. Carson*, 362 U.S. 207, 80 S.Ct. 619 (1960) (holding that a Georgia company had nexus with Florida because it sent brokers to Florida with advertising material who were actively engaged in Florida for the purpose of attracting, soliciting and obtaining Florida customers).

If the Taxpayer has nexus with Tennessee, it will qualify as a dealer under the categories defined below in Tenn. Code Ann. § 67-6-102(12). A "dealer" means every person, as used in this chapter who:

> (I) Has any representative, agent, salesperson, canvasser or solicitor operating in this state, or any person who serves in such capacity, for the purpose of making sales or the taking of orders for sales, irrespective of whether such representative, agent, salesperson, canvasser or solicitor is located here permanently or temporarily, and irrespective of whether an established place of business is maintained in this state;
>
> (J) Engages in the regular or systematic solicitation of a consumer market in this state by the distribution of catalogs, periodicals, advertising fliers, or other advertising, or by means of print, radio or television media, by telegraphy, telephone, computer data base, cable, optic, microwave, or other communication system.

According to Tenn. Code Ann. § 67-6-501(a), a dealer is liable for collecting tax for any sales it makes either inside or outside of Tennessee for use in Tennessee:

> Every dealer making sales, whether within or outside the state, of tangible personal property, for distribution, storage, use, or other consumption in the state, or furnishing any of the things or services taxable under this chapter, is liable for the tax imposed by this chapter.

According to the facts provided by the Taxpayer, title for the product passes at the Taxpayer's location once the order has been completed and billed to the customer, therefore, the Taxpayer's home state has the first right of taxation. Any tax paid in that state will be credited against the amount of tax owed to Tennessee. Tenn. Code Ann. § 67-6-507(a) states that if tax has already been paid on an item of tangible personal property and the amount of tax is less than what would have been paid in Tennessee if the item had been purchased in Tennessee, then the dealer must pay the difference between the amount paid and the amount owed.

Assuming the Taxpayer has nexus with Tennessee, the Taxpayer, as a dealer, is liable for collecting use tax on the initial shipment of goods to Tennessee as well as on any subsequent shipments to Tennessee. The Taxpayer, however, can credit all or a portion of sales taxes paid to the Taxpayer's own state against any Tennessee use tax liability.

2. <u>The Taxpayer is required to collect and remit use tax on any subsequent shipments of research materials to customers in Tennessee. The tax for each set of materials delivered to Tennessee should be collected and remitted at the time when the customer requests shipment to Tennessee and when the Taxpayer charges the customer for shipping and handling for the shipment to Tennessee.</u>

A Tennessee tax liability occurs when the goods are brought into Tennessee for sale at retail, use, consumption, distribution or storage for subsequent use. *Texas Gas Transmission Corp. v. Benson*, 444 S.W.2d 137, 139 (Tenn. 1969). The Taxpayer is required to collect and remit use tax on any subsequent shipments of research materials to customers in Tennessee based on the sales price of the items to be shipped. *Pearle Health Services v. Taylor,* 799 S.W.2d 655 (Tenn. 1990). The tax for each set of materials delivered to Tennessee should be collected and remitted at the time when the customer requests shipment to Tennessee and when the Taxpayer charges the customer for shipping and handling for the shipment to Tennessee. The Taxpayer can credit all or a portion of sales taxes paid to the Taxpayer's own state against any Tennessee use tax liability.

3. <u>The Taxpayer is not required to collect and remit Tennessee sales tax on the shipping charges for any of the shipments as long as the shipping charges are stated separately from any handling fees. The Taxpayer is required to collect and remit Tennessee sales tax on any handling fees.</u>

Where title to the property being transported passes to the vendee at the point of origin, the freight or other transportation charges are not subject to the sales or use tax.[2]

[2]Legislation related to the Streamlined Sales and Use Tax Agreement, effective July 1, 2007, may result in changes regarding the application of sales and use tax sales of certain items of tangible personal property.

TENN. COMP. R. & REGS. 1320-5-1-.71 ("Rule 71") states:

> Freight, delivery, or other like transportation charges are subject to the Sales and Use Tax if title to the property being transported passes to the vendee at the destination point. **Where title to the property being transported passes to the vendee at the point of origin, the freight or other transportation charges are not subject to the Sales or Use Tax**. It is immaterial whether the vendor or vendee actually pays for any charges made for transportation, whether the charges are actually paid by one for the other, or whether a credit or allowance is made or given for such charges. In cases, where a vendor makes a separate charge for delivering tangible personal property in his own vehicle, or makes arrangements for delivering tangible personal property, other than by a common carrier, the delivery charges shall be considered a part of the selling price subject to the Sales or Use Tax. (Emphasis added).

The shipping charges are not subject to sales or use tax because title to the goods passes at the Taxpayer's loading dock, the point of origin. Neither the statutes nor the regulations provide a similar exemption for handling fees. In *Saverio v. Carson*, 208 S.W.2d 1018 (Tenn. 1948), the Tennessee Supreme Court addressed a single charge covering multiple items, in which some items were taxable and some were non-taxable. Specifically, the case involved a laundry operator who rented and laundered diapers. One part of the business was laundering diapers owned by the customers; the other part was renting out laundered diapers owned by the laundry operator. With regard to the rented diapers, the laundry operator argued that she should not be subject to tax on the part of the rental fee that covered the laundering service because a laundry service was exempt from tax. However, the Court found that the rental charge was not divisible and the law required that the tax be based on the gross proceeds from the rental; thus, the exclusion of the non-taxable items from the tax base was not permitted. Similarly under the facts at issue, if the shipping charges and handling fees are not separated, both will be subject to tax. If the shipping charges and handling fees are separated, only the handling fees will be subject to Tennessee sales tax.

David A. Gerregano
General Counsel

Approved: Reagan Farr
Commissioner of Revenue

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